Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C.
701 Pennsylvania Avenue, N.W.
Washington, D.C 20004

One Financial Center
Boston, Massachusetts 02111
Telephone: 617/542-6000
Fax: 617/542-2241

Telephone: 202/434-7300
Fax: 202/434-7400
Telex: 753689

Donna N. Lampert

Direct Dial Number
202/434-7385

EX PARTE OR LATE FILED

July 23, 1996

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BY HAND
William F. Caton
Acting Secretary
Federal Communications Commission
Room 222
1919 M Street, N.W.
Washington, D.C. 20554

Re: CC Docket No. 96-112 - Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services

Dear Mr. Caton:

On July 23, 1996, Jeffrey Sinsheimer, Director of Regulatory Affairs, California Cable Television Association, sent the attached letter to Mr. Daniel Gonzalez, Legal Advisor to Commissioner Chong, regarding the above-referenced docket.

Pursuant to Section 1.1206(a)(1) of the Commission's Rules, two copies of this written document are attached for inclusion in the public record in the above-captioned proceedings.

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Should you have any questions regarding this matter, please contact me.

Sincerely,

Donna N. Lampert

Attachment

cc: John Nakahata
James Coltharp
Anita Wallgren
Regina Keeney
Kathleen Levitz
Anna Gomez
Greg Rosston
Joseph Farrell

F1/56003.1

4341 PIEDMONT AVENUE
P.O. BOX 11080
OAKLAND, CALIFORNIA 94611
(510) 428-2225
FAX (510) 428-0151

JEFFREY SINSHEIMER
Director of Regulatory Affairs

July 23, 1996

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OFFICE OF SECRETARY

Mr. Daniel Gonzalez
Legal Advisor
Office of Commissioner Chong
Federal Communications Commission
Room 844
1919 M Street, N.W.
Washington, D.C. 20554

Re: CC Docket No. 96-112 -- Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming Services

Dear Mr. Gonzalez:

As you have noted, US WEST has proposed a 50/50 subscriber based allocation methodology for incumbent local exchange carriers ("LECs") in response to the Commission's Notice in the above-referenced docket. This proposal is contrary to the law and inconsistent with the sound economic principles of cost causation.

As explained by US WEST, this methodology would mean that common plant "that can be supported solely by telephone needs" would be directly assigned 100% to regulated accounts, additional video costs would be assigned 100% to video and then the common costs would be allocated 50% to video on a per-subscriber basis.[1/] As US WEST concedes, the purpose of this approach is to enable the LECs to enter the video business without requiring them "to absorb heavy losses for an extended period of time."[2/] Without such a mechanism, urges US WEST, "no sensible LEC would introduce video services using common facilities...."[3/]

[1/] See Comments of US WEST, Inc., in CC Docket 96-112, filed May 31, 1996, at 10-11.

[2/] Id. at 9-10.

[3/] Id. at 10.

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The fundamental problem with the US WEST proposal is that, rather than being grounded in sound principles of cost causation, it skews the video marketplace by sending false economic signals about the relative risk of LEC entry into the wired video business. Rather than requiring the LECs to bear the costs of their business decisions to enter the wired video business by utilizing integrated networks, just as they must do when they seek to enter the video business through other means such as wireless cable ("MMDS") or Direct Broadcast Satellites ("DBS"),[4/] the US WEST proposal would require LECs to bear video-related costs only when there is a video customer to offset those costs. This discriminatory approach is inconsistent with the Telecommunications Act of 1996[5/] and contrary to the manner in which the LECs will incur costs to enter the video business using hybrid networks.

As delineated by US WEST, the proposal leaves certain critical questions unanswered. For instance, to the extent the competitive video service fails to attract subscribers, who will bear the burden of the network investment costs? US WEST sets forth an example whereby 1,000 video-capable loops are deployed at a cost of $500,000 and posits a situation where the LEC has only one video customer who would be required to cover $250,000 in costs (under a straight 50% fixed allocator).[6/] While US WEST states this is a "double-whammy,"[7/] the fact is that it never explains why the ratepayers of the regulated telephony service should bear the risk of these investments. Under the US WEST proposal, it appears that shareholders are held harmless in the event the service fails to achieve sufficient penetration. Further, if the investments are never recovered from the nonregulated

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[4/] Indeed, video competitors that seek to enter the video business through DBS are required to bear enormous upfront costs with no special guarantee from regulators that they will not be required to absorb "heavy losses," whether in the start-up or service deployment phases. See, e.g., "Murdoch Adds U.S. to DBS Empire," Broadcasting and Cable, January 29, 1996, at 5 (DBS venture will spend $1.2 billion excluding marketing and advertising costs to get the service up and running).

[5/] Section 254(k), Subsidy of Competitive Services Prohibited, 47 U.S.C. § 254(k) (1996).

[6/] Comments of US WEST, Inc. supra, at 9.

[7/] Id.

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video venture, telephone ratepayers would be required under the US WEST approach to foot the bill, as the loops would never be "actually used" for both video and telephony.[8/]

As CCTA has explained, the law requires that the Commission ensure that telephone ratepayers are no worse off than they would have been had the LECs not decided to pursue the competitive video ventures.[9/] Thus, the crucial question is not whether the common plant can support telephony services, but whether it is necessary for those services and whether the decision to deploy the so-called common plant was driven by video or telephony based needs.

The FCC's cost allocation rules must be based upon the way in which costs are incurred. To the extent the LECs will be required to incur the same common costs whether they have one video subscriber or all potential video subscribers, that should be reflected in a cost allocation methodology consistent with the principles of cost causation.[10/]

CCTA contends that when the FCC approaches these issues in this way, it will find that but for the decision to create video-capable networks, the LECs did not need to deploy the costly hybrid networks that are at issue. Indeed, the economics are such that it is wholly proper for LECs to bear the full costs of their business decisions, even if they have very few customers, as the full range of costs will in fact be incurred in order to provide service even to a few customers. Consequently, while US WEST's preferred approach would fulfil its

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[8/] Id. at 10.

[9/] Comments of California Cable Television Association, CC Docket No. 96-112, filed May 31, 1996, at 5.

[10/] This is the premise of the Commission's Notice as it set forth the following express goals: "administrative simplicity; adaptability to evolving technologies; uniform application among incumbent local exchange carriers . . .; and consistency with economic principles of causation." Notice at ¶ 24. Indeed, this was the basis for CCTA's proposed fixed allocator of 76% to non-regulated, 24% to regulated. See Comments of CCTA, supra, at 17-20.

goal of insulating it from the start-up financial risks of the wired video business, the subscriber-based approach is flawed because it is not related to the manner or reason that these costs were incurred.

Sincerely,

Jeffrey Sinsheimer

Jeffrey Sinsheimer
Director of Regulatory Affairs

cc: John Nakahata
James Coltharp
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